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IN THE

Supreme Court of the United States

OCTOBER TERM—1934.

No. 6

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

against

SUSAN DWIGHT BLISS

BRIEF FOR RESPONDENT.

JAMES McKINLEY ROSE,
Counsel for Respondent.

R. L. VON BERNUTH,
MORRELL S. LOCKHART,
JOHN F. BOYER,
Of Counsel.

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BRIEF FOR RESPONDENT.

This is an appeal on writ of certiorari granted April 30, 1934 (R. 32) from a judgment of the Circuit Court of Appeals for the Second Circuit (R. 31) which reversed an order of the United States Board of Tax Appeals (R. 20) redetermining deficiencies in respondent's income taxes for the years 1928 and 1929.

Opinions Below.

The findings of fact (R. 16, 17) and opinion of the Board of Tax Appeals (R. 18-20) promulgated December 2, 1932 are reported in 27 B. T. A. 205. The opinions of the Circuit Court of Appeals for the Second Circuit (R. 26-31) are reported in 68 Fed. 2d 890. The order granting certiorari (R. 32) is reported in 78 L. Ed. 863.

Statement of Facts.

The proceedings before the Board of Tax Appeals were begun by petitions (R. 2-6; 9-12) to review income tax deficiencies, for the years 1928 and 1929, in the amounts of $1909.31 and $1009.41, respectively, assessed against respondent by the Commissioner of Internal Revenue, as set forth in deficiency letters of the Commissioner, copies of which are annexed to the petitions.

The issues litigated before the Board of Tax Appeals were raised as to the 1928 case by an amended petition (R. 6-7) and an amended answer to the amended petition (R. 7-8) and as to the 1929 case by the petition (R. 9-12) and the amended answer thereto (R. 12-13).

In the amended answers (paragraphs 4 and 6, respectively) before the Board of Tax Appeals, the Commissioner for the first time questioned the amount of charitable contributions claimed as a deduction by respondent, and alleged that the deductions allowed by him for charitable contributions upon the audits of respondent's tax returns for said years were excessive (R. 8, 12, 13).

Prior to the hearing before the Board of Tax Appeals the respondent and the Commissioner entered into stipulations in both cases (1928: R. 13-14; 1929: R. 15) disposing of all questions except the one now before this court and agreeing upon the facts relevant to this question. The stipulations are summarized in the government's statement of facts. At the hearing the cases were consolidated and have been treated as one case throughout the subsequent litigation.

Questions Presented.

One question only was presented to the court below for its opinion and one question only is involved on this appeal:

May the taxpayer deduct charitable contributions up to 15% of net income (as defined by Section 21 of the Revenue Act of 1928), or only up to 15% of net income

less capital gains, if the taxpayer has elected to be taxed on capital net gains under the provisions of Section 101 of said act.

The respondent contends that under the provisions of Sections 21 and 23-n of said act the taxpayer is entitled to deduct charitable contributions up to 15% of total net income irrespective of her election as to the taxation of her capital net gains under Section 101 of said Act.

The Commissioner, on the other hand, contends that if the taxpayer elects to be taxed on capital net gain at the flat rate provided by Section 101, deductions for charitable contributions should be limited to 15% of "ordinary net income", which is computed after excluding from net income (and hence from gross income from which such net income is determined) all taxable net capital gain.

The difference in respondent's income tax liability for the years 1928 and 1929 under these two contentions is shown by the following tabulation:

As to the year 1928	*Respondent's Computation*	*Commissioner's Computation*
(a) Net Income as defined by Section 21 without deducting charitable contributions allowed by Section 23-n	$482,035.59	$482,035.59
(b) Capital net gain as computed under Section 101(c) (5)		211,544.82
(c) "Ordinary net income" as computed under Section 101(c) (7) without allowance for charitable contributions		270,490.77
(d) Limit of deduction for charitable contributions allowed by Section 23-n		
Respondent's contention (15% of (a))	72,305.34	
Commissioner's contention (15% of (c))		40,573.62
(e) Total contributions made by Respondent	43,995.92	43,995.92
(f) Deficiency of taxable income claimed by Commissioner		3,422.30

As to the year 1929	*Respondent's Computation*	*Commissioner's Computation*
(a) Net income, as defined by Section 21, without deducting charitable contributions allowed by Section 23-n	$547,514.14	$547,514.14
(b) Capital net gain as computed under Section 101(c) (5)		299,942.31
(c) "Ordinary net income" as computed under Section 101(c) (7) without allowance for charitable contributions		247,571.83
(d) Limit of deduction for charitable contributions allowed by Section 23-n		
Respondent's contention (15% of (a))	82,127.12	
Commissioner's contention (15% of (c))		37,135.77
(e) Total contributions made by Respondent	39,088.46	39,088.46
(f) Deficiency of taxable income claimed by Commissioner		1,952.69

Statutes Involved.

The pertinent provisions of the Revenue Act of 1928, under which this case must be decided, are set forth in the Appendix, *infra,* pages 21-27. The title headings as they appear in the Statute have been retained in the Appendix, as they are necessary for an understanding of the question here involved.

Summary of Argument.

The controlling provisions of the Revenue Act of 1928 are to be found in Sections 21, 22 and 23 which define for all purposes of the Act gross income, net income and deductions from gross income, including deductions for charitable contributions. Section 23(n) limits the deduction for charitable contributions to 15% of taxpayer's net income, which is defined by Section 21 to be gross income, computed under Section 22, including all capital gains, less the deductions, allowed by Section 23. This is the only pro-

vision in the Act concerning deductions for charitable contributions and must govern every case in which such deduction is taken. Unless these sections are modified by some provision of Section 101 or the other sections dealing with capital gains and losses, capital gains must be included in determining the amount of net income from which the 15% limitation for charitable contributions is determined.

Section 101 does not modify the provisions of Sections 21, 22 and 23 determining the amount of taxpayer's net income and allowable deductions. The Revenue Act of 1928 is divided by title headings which are a guide to the proper construction of its sections. Subtitle B—Part I and the corresponding Supplement A of Subtitle C, dealing with capital gain and losses, are concerned solely with rates of tax. Subtitle B—Part II and the corresponding Supplement B of Subtitle C are concerned with the computation of net income. Section 101 is contained in Supplement A (rates of tax) whereas Sections 21, 22 and 23 are contained in Subtitle B—Part II (computation of net income). Reference is made to the Appendix hereto (*infra*, pp. 21-27), which shows that the Act is divided in such manner as to indicate the respective application of the various sections.

The construction placed upon the Act by respondent is required by the wording of the statute. It has been sustained by every court which has passed on the point and is supported by the evident intention of Congress as found in the reports of Committees, the interpretation of judges and the repeated passage of pertinent provisions of the Act in identical language after administrative interpretation thereof in accordance with respondent's contention.

The fact that Congress did not make clear an intention to exclude capital net gains from the base upon which the limitation for contributions is computed when it might very easily have done so by a simple express provision, is strong evidence that Congress did not intend that the charitable contribution provisions of the Act should be modified by the capital gain provisions. Both provisions were included for the purpose of relieving the taxpayer of excessive tax

burdens and encouraging him, on the one hand, to make contributions, and on the other, to realize his capital gains. It is not likely that Congress intended to allow the taxpayer the advantage of one such provision only at the cost of losing the advantage of the other.

ARGUMENT.

POINT I.

Respondent was entitled to deduct charitable contributions to the extent of fifteen percent of total net income including capital net gains.

The essential conflict between respondent's position and that of the Commissioner lies in the interpretation of Section 23-n, which reads:

> "Section 23 (26 U. S. C. A. Section 2023) In computing net income there shall be allowed as deductions:
> * * * * * * *
> (n) *Charitable and other contributions:* In the case of an individual, contributions or gifts made within the taxable year * * * to an amount which in all the above cases combined does not exceed 15 percentum of the taxpayer's net income as computed without the benefit of this sub-section. * * *"

This is the only provision in the Revenue Act of 1928 dealing specifically with deductions for charitable contributions and must govern all cases in which such deductions are claimed. A proper interpretation of Section 23(n) requires that it be read with Sections 21 and 22 of the same Act.

Section 21 defines net income for all purposes of the Act, as follows—

> "Section 21 (26 U. S. C. A., Section 2021) 'Net income' means the gross income computed under Section 22, less the deductions allowed by Section 23."

Section 22 defines "gross income" as follows:

> "Section 22 (26 U. S. C. A., Section 2022) 'Gross income' includes gains, profits, * * * and income derived from any source whatever."

Capital net gains are a part of gross income and, except as they may be reduced by the deductions allowed by Section 23, are also a part of net income. By Section 23-n, read in connection with Sections 21 and 22, charitable contributions are, therefore, a direct deduction from gross income including capital net gain, the amount of such deduction being limited only by the provision that it shall not exceed 15% of the taxpayer's net income, which also includes capital net gain.

The above sections are all contained under Sub-title B, Part II, entitled "Computation of Net Income." There are no provisions in Sub-title C which is supplementary to the provisions of Sub-title B, which limit, or modify in any way, the applicability of the above definitions to the determination of respondent's net income.

Section 101 is contained in Sub-title C, Supplement A—entitled "Rates of Tax [Supplementary to Sub-title B, Part I]", and has no application to the computation of gross or net income or deductions from gross income, contained in Sub-title B, Part II. It affects solely the amount and rate of tax on such part of net income, already computed under the prior sections of the act, as is allocable to capital net gains and losses. It concerns the computation of a tax on a specific kind of net income, not a computation of net income subject to tax.

This appears from the headings under which the Act is arranged. Sub-title B, Part I is entitled "Rates of Tax". Sec. 11, "Normal Tax on Individuals", and Sec. 12, "Surtax on Individuals", in Part I, relate to the normal and surtaxes on individuals, and in Sec. 12 appears the following:

> "(c) Capital Net Gains and Losses.—For rate and computation of tax in lieu of normal and surtax in case of net incomes of not less than $30,000, ap-

> proximately, or in case of net incomes, excluding items of capital gain, capital loss and capital deductions, of not less than $30,000, approximately, see section 101."

Subtitle B, Part II is entitled "Computation of Net Income", and contains Sections 21, 22 and 23. Part II says nothing as to the exclusion of capital gains or losses in the computation of net income.

Subtitle B also contains Parts III, IV and V which respectively deal with "Credits against Tax", "Accounting Periods and Methods of Accounting" and "Returns and Payment of Tax".

Subtitle C bears the general heading "Supplemental Provisions" and contains subdivisions headed, respectively, Supplements A, B, C and D, which in each instance are stated to be supplemental to Parts I, II, III and V, respectively, of Subtitle B. Supplement A is entitled "Rates of Tax" (Supplementary to Subtitle B, Part I, the rate of tax part of Subtitle B), and it is under this supplement that Section 101, relating to the rate of tax on capital net gains and losses is placed. Supplement B is entitled "Computation of Net Income" (Supplementary to Subtitle B, Part II), and its provisions deal exclusively with the method of arriving at gain or loss, including capital gain or loss, and say nothing about segregating capital net gain from the computation of net income. It is apparent, therefore, that such segregation is by the form of the statute made for the purpose of applying a different rate of tax to such capital gains, as expressly provided for by subdivision c of Section 12, cannot affect the deductions to which the taxpayer is entitled under Section 23 of Subtitle B, Part II, relating to the computation of net income.

The government contends, in its brief, that if the taxpayer elects to be taxed under Section 101 (a) the words "ordinary net income" (as defined by Section 101 (c)—(7)) must by implication be substituted for the words "net income" in Section 23 (n), so that charitable contributions will be limited to fifteen percent of "ordinary net

income'' instead of fifteen percent of net income. In support of this contention the government argues that Section 101 contains specific provisions dealing with taxpayer's allowable deductions in such cases which supersede the general provisions of Sections 21, 22 and 23. The government also reads into Section 101 an intention, not apparent from the wording thereof, that capital gains shall be segregated from ''ordinary net income'' for all purposes of the Act. The fallacy of this contention is apparent when one considers the scope of Section 101 as defined by the headings under which it appears as above discussed. In its brief the government omits these headings and treats the Act as though there were no distinction between the provision for rates of taxation and those for the computation of income. Appendix A to the government's brief also omits, except in respect to Sections 21, 22 and 23, the Subtitle headings applicable to the sections. This omission is indicative of the error into which the government has fallen. The distinction is inherent in the Act and a recognition of it is essential to an interpretation of the statute. The entire force of the government's argument is spent by reason of its ignoring the title headings. The provisions of Supplement A of Subtitle C, which contains Section 101 are supplementary to the provisions of Subtitle B—Part I and purport to deal only with the rate of tax on net income where capital net gains are included therein. To read into this section an intention to alter the meaning of the prior provisions of Subtitle B—Part II defining gross income, net income, and deductions from net income is to ignore the express wording of the statute. This is further borne out by the fact that the provisions of Supplement B of Subtitle C, Supplementary to Subtitle B—Part II, relating to the computation of net income, contain no provisions whatsoever altering the definitions of net income and gross income, or changing the allowable deductions.

Section 101 gives the taxpayer an election to have his income derived from capital net gain taxed at a different rate from that applied to income derived from other sources. The taxpayer may divide his taxable *net income*

into two parts. The first represents all such income from sources other than capital net gain and on this part he pays a tax computed at the usual rates provided under the earlier sections of the Act. For convenience of nomenclature this part is called "ordinary net income". On the balance of his net income, consisting solely of capital net gain, the taxpayer pays a tax at a flat rate of 12½%. The words "ordinary net income" are used solely to differentiate income derived from other sources of revenue than capital net gain for the purpose of fixing a tax thereon.

As an additional argument in support of the construction which it seeks to place on Section 101, the government states at page 16 of its brief: "Sections 11 and 12 of the 1928 Act (infra, p. 27) levy a normal tax and a surtax on the taxpayer's 'net income', but where the capital gain provisions are applied 'net income' as used in those sections is taken to mean 'ordinary net income' ". This statement is erroneous. Where the capital gain provisions are applied, Sections 11 and 12 are superseded by Section 101 (a), which directs that

> "there shall, at the election of the taxpayer, be levied, collected and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted and the total tax shall be this amount plus 12½ per centum of the capital net gain."

There is no implied modification of the meaning of "net income" as used in Sections 11 and 12 but an express provision dividing such net income into its component parts and providing new rates of tax therefor.

There is nothing in Section 101, supplementing Subtitle B, Part I, which either expressly or by implication changes the definitions of net income, gross income, or deductions from gross income contained in Sections 21, 22 and 23 under Subtitle B, Part II, nor is there anything to that

effect in the provisions of Sections 111 to 120 which do supplement Subtitle B—Part II.

Nor does Section 23-n, either expressly or by implication, limit deductions for charitable contributions to 15% of "ordinary net income". On the contrary it specifically authorizes such deductions up to 15% of "net income".

The contention of the respondent as to the proper interpretation of the law has been upheld by every court which has passed on the question, including the final determination of the full membership of the Board of Tax Appeals.

> *White* v. *Atkins*, C. C. A. 1st., 69 Fed. 2nd 960
> Affirming *Atkins* v. *White*, 3 Fed. Supp. 694;
> *Blow* v. *United States*, N. D. Ill., 5 Fed. Supp. 737;
> *Straus* v. *Commissioner*, 27 B. T. A. 1116.

This was also the view of the majority of the Circuit Court of Appeals for the Second Circuit in the case below.

> *Bliss* v. *Commissioner*, 68 Fed. 2nd, 890 (R. 26-29).

In this case, Judge Swan, who rendered the majority opinion, said at page 892:

> "There is nothing in section 101 which expressly indicates that the taxpayer was intended to lose any part of the deductions allowed by section 23 when his tax is determined according to the rates provided in section 101. Paragraphs (a) and (b) deal with computation of the tax rather than with computation of taxable income; the usual rates are applied, 'as if this section had not been enacted', to that part of the taxable income called 'ordinary net income' and the special 12½ percent rate to 'capital net gain' or 'capital net loss.' Paragraph (c) defines the terms used in the earlier paragraphs. It does not indicate an intention to modify the definitions of 'net' and 'gross' income contained in sections 21 and 22 (26 U. S. C. A. §§ 2021, 2022), nor to change the deductions allowed by section 23 (26 U. S. C. A. § 2023). On the contrary, clauses (3) and (4) of section 101 indicate that they are to remain unchanged. They divide

> such deductions into 'capital deductions' and 'ordinary deductions.' The latter mean 'the deductions allowed by section 23 other than capital losses and capital deductions.' Clause (5) defining 'capital net gain' makes it necessary to determine whether 'ordinary deductions' exceed 'gross income computed without including capital gains.' We do not understand this to be a direction that in computing 'ordinary deductions' gross income is to be decreased by the exclusion of capital gains. It means to us that ordinary deductions are to be figured in the ordinary way and then compared with 'gross income computed without including capital gain' to see if they exceed it. If this be the correct construction, there is harmony between clause (5) and clause (7), and 'net income' computed in accordance with sections 21, 22, and 23 is composed of two parts, 'ordinary net income' and 'capital net gain', to which respectively the appropriate rates may be applied as provided in paragraph (a)".

In *Straus* v. *Commissioner*, 27 B. T. A. 1116, (pending after argument on petition for review in the Court of Appeals, District of Columbia) the Board of Tax Appeals, reversing its previous decisions and holding that capital net gains should be included in computing the allowable deduction for charitable contributions, said concerning the construction of Section 101 at page 1121:

> "Apparently the Commissioner places his chief reliance upon the language of section 101 (c) (7), which is as follows:
>
> > '"Ordinary net income" means the net income, computed in accordance with the provisions of this title, after excluding all items of capital gain, capital loss, and capital deductions.'
>
> This language does not mean that net income is to be *computed* after excluding certain items of a capital nature. It means that 'net income' is to be computed in the regular way and 'ordinary net income' is what remains of this 'net income' after the capital items have been excluded from it. This is clearly indicated by the punctuation used by Con-

gress. The phrase 'computed in accordance with the provisions of this title' is set off by commas and modifies 'net income'. Section 101 (c) (7) is not to be read as if one or both of the first two commas had been omitted, or as if it provided that ordinary net income means net income computed after excluding all items of a capital nature. 'This title' means Title I. Net income computed in accordance with Title I is obviously net income as defined in section 21 of Title I, i. e., gross income as defined in section 22 less the deductions allowed by section 23. There is in section 101 (c) (7) no further limitation on the deduction for contributions beyond that contained in section 23 (n). Since there is nothing to indicate that Congress had this subject in mind while framing this section, we should be slow to read the intent into the words used by Congress on an unrelated subject. We may not read this thought into the statute where the words used do not contain it. Note the difference in section 101 (c) (5), where Congress used the words 'gross income computed without including capital gains.'

'Capital net gain' means the excess of the total amount of capital gain over the sum of (A) the capital deductions and capital losses, plus (B) the amount, if any, by which the ordinary deductions exceed the gross income computed without including capital gains.

If Congress, in section 101 (c) (7) had used the words 'net income computed without including capital gain' the Commissioner would be supported in his contention. But it did not use these words or any of like import."

See also

White v. *Atkins*, 69 Fed. 2d, 960, at page 963.

The foregoing construction of Section 101 accords with the scheme of the Revenue Act of 1928 as expressed in other sections. Throughout the Act Congress has provided for the taxation of various portions of net income at special rates, exempting parts thereof entirely, depending upon the circumstances in the case of each individual taxpayer. Examples are to be found in Section 31, which provides for

the segregation of a portion of net income to be known as "earned income" to be taxed at a lower rate, and in Section 25, which provides for credits against net income, in computing normal tax, of dividends from domestic corporations and interest on certain United States obligations. Sections of this character in no way affect the amount of "net income" upon which the deduction of 15% for charitable contributions is based. Section 101 is only another instance in the Act where a specific portion of "net income" is taxed at a special rate and is not pertinent to the construction of Sections 21, 22 or 23 (n).

The government cites the case of *Westfeldt* v. *Commissioner*, 63 Fed. 2nd, 882, in support of its theory that segregation of capital net gains from "ordinary net income" is, under the provisions of Section 101, made complete for all purposes of the Act. That case is no authority for the theory, as the segregation there referred to was merely for the purpose of applying the proper rates of tax to the various classes of income involved. It should be noted that the statute applicable to that case (Section 207 (b), Revenue Act of 1924) specifically provided that the partnership income there in question should be added to "the other income of the taxpayer *subject to such rates*" (i. e., the ordinary rates for income during the year 1924). Neither the facts nor the language of the case is authority for the broad interpretation which the government seeks to place on Section 101.

The government cites and argues from the decision of the Board of Tax Appeals in *Elkins* vs. *The Commissioner*, 24 B. T. A. 572. We believe that the principles involved in this decision might be sustained upon considerations other than those involved in this case. The *Elkins* case involved capital net loss. Insofar as the principles governing capital net gain and capital net loss are the same, we believe the *Elkins* decision is unsound.

POINT II.

The construction of the Act by the Court below is in accordance with the Congressional intent.

The purpose of Section 101 has been stated by Mr. Justice Stone in *Burnet* v. *Harmel,* 287 U. S. 103, 106; 77 L. Ed. 199, 202 to be:

> "to relieve the taxpayer from these excessive tax burdens on gains resulting from a conversion of capital investments and to remove the deterrent effect of these burdens on such conversions."

citing House Report, No. 350, Ways and Means Committee, 67th Congress, First Session, on the Revenue Bill of 1921, page 10.

Similarly, the purpose of Section 23-n was stated by Judge Swan in the majority opinion in the case below, 68 Fed. 2nd, 890, at page 891 (R. 27), as follows:

> "The provision permitting a deduction from gross income of charitable contributions to the extent of 15 percent of the net income computed without the benefit of this deduction was introduced into the income tax law by section 1201(2) of the Revenue Act of 1917 (40 Stat. 330). Its obvious purpose was to encourage gifts for charity, education, and science (Cong. Rec., September 7, 1917, p. 5728). It has been continued in substantially the same form in each successive revenue act."

A construction which permits the taxpayer to have his capital gains taxed at a flat rate only at the cost of decreasing the benefit of the deductions for charitable contributions allowed by Section 23 (n) is in direct contravention of the purposes of Section 101 and of Section 23-n so expressed.

It should be noted that had Congress intended the result sought by the Commissioner it could have achieved it simply and conclusively by providing affirmatively in Sub-title B—Part II of the act that capital net gain should be excluded

from net income (as defined by Section 21) if the taxpayer elected to be taxed thereon under Section 101.

Instead, Congress reenacted the capital gain and loss provisions first appearing in the 1921 Act in almost identical language in the 1924, 1926 and 1928 Acts. These reenactments were subsequent to and therefore a legislative approval of the construction previously placed upon the words of Congress by the Commissioner.

Brewster v. *Gage*, 280 U. S. 327.
United States v. *Falk*, 204 U. S. 143.
National Lead Co. v. *United States*, 252 U. S. 140.

In *White* v. *Atkins*, 69 Fed. 2d, 960, the Circuit Court of Appeals for the First Circuit, affirming the District Court decision of *Atkins* v. *White*, 3 Fed. Supp., 694, on facts similar to those of the case at bar, said at page 962—

> "There is nothing to indicate that Congress by the enactment of this provision for taxing capital net gains in the 1921 Act, in order to encourage greater activity in the sale of capital assets, intended thereby in any way to change the amount deductible for charitable contributions by limiting them to 15 per cent. of the individual's 'ordinary net income' instead of his net income as hitherto. The result is inconsistent with the purpose for which the deduction was allowed in the 1917 Act. If Congress had so intended by the provision for a flat rate assessment of capital gains, it would, we think, have made its intent clear. It has never done so.
>
> * * * We find no logical ground, derived from the history or prior construction of these acts, for holding that 'ordinary net income' as defined in Section 101 of the 1928 Act * * * is the base for limiting the deduction of contributions for charitable purposes under Section 23 (n) * * * .
>
> It is made clear in the 1932 Act that the provisions for the assessment of taxes when capital net gains and losses are involved are entirely separate from, and have no relation to, Sections 21, 22 and 23 of Part 2 of that Act. * * * Sub-title C * * * under which the provisions relating to capital net gains and

> capital net losses are found, provides that these provisions are merely supplementary to subtitle B in part 1 * * * which relates solely to rates and not to the manner of determining net income."

The Commissioner of Internal Revenue so interpreted the Congressional intent in applying the identical provisions of the 1921, 1924, 1926 and 1928 Revenue Acts prior to the decision of the Board of Tax Appeals in 1931 in *Elkins* v. *Commissioner,* 24 B. T. A. 572, involving capital net loss. The Court below summarized the acts of the Commissioner as follows (R. 29):

> "On February 6, 1923, the Deputy Commissioner telegraphed in response to an inquiry: 'Contributions; 15% limitation; Capital net gains: fifteen percent. limitation for deductions account charitable contributions applies to total net income inclusive of gain from sale of capital assets' (C. C. H. Fed. Income Tax Service, 1924, par. 2033). In 1924 a corresponding ruling as to capital losses was made: 'Capital losses cannot be excluded in computing net income for the purpose of determining the amount of charitable contribution deductions' (I. T. 404, Cum. Bul. III-2, p. 152). In 1928 the Government argued before this court that section 206 of the Revenue Act of 1921 (42 Stat. 232) (corresponding to section 101 of the 1928 act (26 U. S. C. A., § 2101)) related merely to rates and did not affect the computation of the allowance of charitable deductions, and we by dictum approved this construction (*Sadowsky* v. *Anderson* (C. C. A.) (29 F. (2d) 677, 679)). In November 1931 the Board of Tax Appeals decided *Elkins* v. *Com'r* (24 B. T. A. 572), and held, contrary to the ruling of the Bureau, that capital losses should be disregarded in computing the 15 percent. deduction for charitable contributions. The Commissioner announced that this decision was 'contrary to the position which the Bureau has consistently followed', and would be appealed (Int. Rev. Bul. XI-7, 5386; Mim. 3931)."

The same construction has been followed by the Board of Tax Appeals since the decision in 1933 in *Straus* v. *Com-*

missioner, 27 B. T. A. 1116, in which the Board, sitting as a whole, overruled the prior decisions of its individual members in the case at bar, *Colgate* v. *Commissioner,* 27 B. T. A. 506, and *Harbison* v. *Commissioner,* 26 B. T. A. 896, each of which involved capital net gain.*

The present change of position of the Commissioner is without basis in any court decision or reasonable rule of construction.

If there be any ambiguity in the statute it should be construed most strongly against the Commissioner and in favor of the purpose of the act as already defined by the courts.

Gould v. *Gould,* 245 U. S. 151, 62 Law Ed. 211.

United States v. *Updike,* 281 U. S. 489, 74 Law Ed. 984.

Old Colony R. Co. v. *Commissioner,* 284 U. S. 552, 76 Law Ed. 484.

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* For the information of the Court we list here every case involving capital net gains which has come to our attention with its present status. Aside from the case at bar, these are:

Harbison v. *Commissioner,* C. C. A. 2d, 68 Fed. (2d) 1004, reversing 26 B. T. A. 896, certiorari granted *sub nom. Helvering* v. *Harbison,* 78 Law Ed. 863, No. 7, October Term 1934, to be argued together with case at bar.

Colgate v. *Commissioner,* C. C. A. 2d, unreported, reversing 27 B. T. A. 506, certiorari granted *sub nom. Helvering* v. *Colgate,* 78 Law Ed. 863, No. 8, October Term 1934.

White v. *Atkins* C. C. A. 1st, 69 Fed. 2d, 966, affirming *Atkins* v. *White,* District Mass. 3 Fed. Supp. 694.

Blow v. *United States,* Northern District Ill. 5 Fed. Supp. 737, pending after argument on appeal to the Circuit Court of Appeals for the Seventh Circuit.

Straus v. *Commissioner,* 27 B. T. A. 1116 pending after argument on petition for Review in Court of Appeals, District of Columbia.

Robinette v. *Commissioner,* 27 B. T. A. 1426 pending after argument on petition for review in the Circuit Court of Appeals, for the Third Circuit.

Iglehart v. *Commissioner,* 27 B. T. A. 1426, pending after argument on petition for review in the Circuit Court of Appeals for the Seventh Circuit.

Woodward v. *Commissioner,* 27 B. T. A. 1426, pending on petition for review in the Circuit Court of Appeals for the Second Circuit.

POINT III.

The judgment of the Circuit Court of Appeals for the Second Circuit should be affirmed.

Respectfully submitted,

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APPENDIX.

Revenue Act of 1928, c. 852, 45 Stat. 791:

TITLE I—INCOME TAX.

SUBTITLE B—GENERAL PROVISIONS.

Part I—Rates of Tax.

SEC. 11. NORMAL TAX ON INDIVIDUALS.

There shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax equal to the sum of the following:

(Here follows list of rates)

SEC. 12. SURTAX ON INDIVIDUALS.

(a) **Rates of surtax.**—There shall be levied, collected, and paid for each taxable year upon the net income of every individual a surtax as follows:

(Here follows list of rates)

* * * * * * *

(c) **Capital net gains and losses.**—For rate and computation of tax in lieu of normal and surtax in case of net incomes of not less than $30,000, approximately, or in case of net incomes, excluding items of capital gain, capital loss, and capital deductions, of not less than $30,000, approximately, see section 101.

* * * * * * *

Part II—Computation of Net Income.

SEC. 21. NET INCOME.

'Net income' means the gross income computed under section 22, less the deductions allowed by section 23.

SEC. 22. GROSS INCOME.

(a) **General Definition.**—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of what-

ever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

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SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * * *

(n) **Charitable and other contributions.**—In the case of an individual, contributions or gifts made within the taxable year to or for the use of:

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(2) Any corporation, or trust, or community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, * * *;

* * * * * * *

to an amount which in all the above cases combined does not exceed 15 per centum of the taxpayer's net income as computed without the benefit of this subsection. * * *.

* * * * * * *

SEC. 25. CREDITS OF INDIVIDUAL AGAINST NET INCOME.

There shall be allowed for the purpose of the normal tax, but not for the surtax, the following credits against the net income:

(a) **Dividends.**—The amount received as dividends—

(1) from a domestic corporation, or

(2) from a foreign corporation when it is shown to the satisfaction of the Commissioner * * *

(specifying conditions under which credit will be allowed)

* * * * * * *

(b) **Interest on United States Obligations.**—The amount received as interest upon obligations of the United States which is included in gross income under section 22.

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Part III—Credits Against Tax.

SEC. 31. EARNED INCOME CREDIT.

(a) **Definitions.**—For the purposes of this section—

(1) 'Earned income' means wages, salaries, professional fees, and other amounts received as compensation for personal services actually rendered, but does not include that part of the compensation derived by the taxpayer for personal services rendered by him to a corporation which represents a distribution of earnings or profits rather than a reasonable allowance as compensation for the personal services actually rendered. In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income producing factors, a reasonable allowance as compensation for the personal services actually rendered by the taxpayer, not in excess of 20 per centum of his share of the net profits of such trade or business, shall be considered as earned income.

(2) 'Earned income deductions' means such deductions as are allowed by section 23 for the purpose of computing net income, and are properly allocable to or chargeable against earned income.

(3) 'Earned net income' means the excess of the amount of the earned income over the sum of the earned income deductions. If the taxpayer's net income is not more than $5,000, his entire net income shall be considered to be earned net income, and if his net income is more than $5,000, his earned net income shall not be considered to be less than $5,000. In no case shall the earned net income be considered to be more than $30,000.

(b) Allowance of Credit.—In the case of an individual the tax shall be credited with 25 per centum of the amount of tax which would be payable

if his earned net income constituted his entire net income; but in no case shall the credit allowed under this subsection exceed 25 per centum of his normal tax plus 25 per centum of the surtax which would be payable if his earned net income constituted his entire net income. This credit shall be in addition to all other credits against the tax.

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Part IV—Accounting Periods and Methods of Accounting.

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Part V—Returns and Payment of Tax.

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SUBTITLE C—SUPPLEMENTAL PROVISIONS.

Supplement A—Rates of Tax.

(Supplementary to Subtitle B, Part I.)

SEC. 101. CAPITAL NET GAINS AND LOSSES.

(a) **Tax in case of capital net gain.**—In the case of any taxpayer, other than a corporation, who for any taxable year derives a capital net gain (as hereinafter defined in this section), there shall, at the election of the taxpayer, be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted and the total tax shall be this amount plus 12½ per centum of the capital net gain.

(b) **Tax in case of capital net loss.**—In the case of any taxpayer, other than a corporation, who for any taxable year sustains a capital net loss (as hereinafter defined in this section), there shall be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the

manner as if this section had not been enacted, and the total tax shall be this amount minus 12½ per centum of the capital net loss; but in no case shall the tax of a taxpayer who has sustained a capital net loss be less than the tax computed without regard to the provisions of this section.

(c) **Definitions.**—For the purposes of this title—

(1) "Capital gain" means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921.

(2) "Capital loss" means deductible loss resulting from the sale or exchange of capital assets.

(3) "Capital deductions" means such deductions as are allowed by section 23 for the purpose of computing net income, and are properly allocable to or chargeable against capital assets sold or exchanged during the taxable year.

(4) "Ordinary deductions" means the deductions allowed by section 23 other than capital losses and capital deductions.

(5) "Capital net gain" means the excess of the total amount of capital gain over the sum of (A) the capital deductions and capital losses, plus (B) the amount, if any, by which the ordinary deductions exceed the gross income computed without including capital gains.

(6) "Capital net loss" means the excess of the sum of the capital losses plus the capital deductions over the total amount of capital gain.

(7) "Ordinary net income" means the net income, computed in accordance with the provisions of this title, after excluding all items of capital gain, capital loss, and capital deductions.

(8) "Capital assets" means property held by the taxpayer for more than two years * * *.

* * * * * * *

(d) **Collection and payment of tax.**—The total tax determined under subsection (a) or (b) shall be collected and paid in the same manner, at the same time, and subject to the same provisions of law, including penalties, as other taxes under this title.

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Supplement B—Computation of Net Income.

(Supplementary to Subtitle B, Part II.)

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SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) **General rule.**—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(Here follow directions as to the methods of determining gain or loss.)

* * * * * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) **Property Acquired After February 28, 1913.**—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

(Here follows enumeration of exceptions.)

* * * * * * *

(b) **Property Acquired before March 1, 1913.**—The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be:

(Here follows description of methods.)

* * * * * * *

SEC. 120. UNLIMITED DEDUCTION FOR CHARITABLE AND OTHER CONTRIBUTIONS.

In the case of an individual if in the taxable year and in each of the ten preceding taxable years the amount of the contributions or gifts described in section 23 (n) plus the amount of income, war-profits, or excess-profits taxes paid during such year in respect of preceding taxable years, exceeds 90 per centum of the taxpayer's net income for each such year, as computed without the benefit of section 23(n), then the 15 per centum limit imposed by such section shall not be applicable.

Supplement C—Credits Against Tax.

(Supplementary to Subtitle B, Part III.)

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Supplement D—Returns and Payment of Tax.

(Supplementary to Subtitle B, Part V.)

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Revenue Act of 1924, c. 234, 43 Stat. 253:

SEC. 207. (b) If a fiscal year of a partnership begins in one calendar year and ends in another calendar year, and the law applicable to the second calendar year is different from the law applicable to the first calendar year, then (1) the rates for the calendar year during which such fiscal year begins shall apply to an amount of each partner's share of such partnership net income (determined under the law applicable to such calendar year) equal to the proportion which the part of such fiscal year falling within such calendar year bears to the full fiscal year, and (2) the rates for the calendar year during which such fiscal year ends shall apply to an amount of each partner's share of such partnership net income (determined under the law applicable to such calendar year) equal to the proportion which the part of such fiscal year falling within such calendar year bears to the full fiscal year. In such cases the part of such income subject to the rates in effect for the most recent calendar year shall be added to the other income of the taxpayer subject to such rates and the resulting amount shall be placed in the lower brackets of the rate schedule applicable to such year, and the part of such income subject to the rates in effect for the next preceding calendar year shall be placed in the next higher brackets of the rate schedule applicable to such year.

(U. S. C., Title 26, Sec. 938.)